

Machinery and equipment that are used primarily in the manufacturing or assembling of tangible personal property for wholesale or retail sale or lease is exempt from Retailers' Occupation Tax. See 86 Ill. Adm. Code 130.330. (This is a GIL).

September 5, 2000

Dear Xxxxx:

This letter is in response to your letter dated June 15, 2000. We apologize for the delay in responding to your inquiry. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120 subsections (b) and (c), which can be found at the Department's website located at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter, you have stated and made inquiry as follows:

Our client has asked us to request a general information ruling with the state of Illinois relating to sales tax.

Facts

The client has contracts to paint newly manufactured replacement parts for several farm equipment manufacturers. The new parts are shipped to our client for painting. The manufacturers own a majority of the parts. We estimate that our client owns 10% of the parts.

The paint-line process—the part is hooked to a conveyer line and pulled through a washer and then through an enclosed painting area (paint booth). Each part receives one coat of paint. The part is pulled through a drying process to dry the paint.

Our client owns the paint and the paint-line equipment. After each part is painted and dried, it is packaged and crated. The part is either shipped directly to the dealer or back to the manufacturer. Our client invoices the manufacturer for the work done. The labor, paint and overhead are not separately stated on the invoice.

Questions

1. Is the paint-line a manufacturing process?
2. Would the paint be exempt from sales tax when purchased?

3. Would the paint-line equipment and replacement parts for the paint-line equipment be exempt from sales tax when purchased?
4. Would the paint booth be exempt from sales tax as either part of the manufacturing process or a pollution control facility?

If you should need further information or have questions, please feel free to contact me at the above phone number or address.

MANUFACTURING MACHINERY & EQUIPMENT EXEMPTION

Machinery and equipment that are used primarily in the manufacturing or assembling of tangible personal property for wholesale or retail sale or lease is exempt from Retailers' Occupation Tax. See the enclosed copy of 86 Ill. Adm. Code 130.330. The manufacturing process is the production of any article of tangible personal property, whether such article is a finished product or an article for use in the process of manufacturing or assembling a different article of tangible personal property, by procedures commonly regarded as manufacturing, processing, fabricating, or refining that changes some existing material or materials into a material with a different form, use, or name. These changes must result from the process in question and be substantial and significant.

As noted in subsection (e)(3) of Section 130.330, the exemption is not generally available for equipment which is used in the performance of a service, since service work does not typically involve the production of tangible personal property for sale or lease. However, the exemption is available to persons considered servicemen, when they perform assembly or fabrication work for a customer, as long as the goods are produced or assembled for sale or lease, rather than for use or consumption.

The use of machinery and equipment to convey, handle, or transport the tangible personal property to be sold within production stations on the production line or directly between such production stations or buildings within the same plant constitutes an exempt use under the manufacturing machinery and equipment exemption. However, the exemption does not extend to machinery or equipment used to store, convey, handle or transport materials or parts or sub-assemblies prior to their entrance into the production cycle. See Section 130.330(d)(4)(C). Nor does the exemption extend to machinery or equipment used to store, convey, handle or transport finished tangible personal property after the completion of the production cycle. See Section 130.330(d)(4)(D).

Please note the exemption does not apply to hand tools, coolants, lubricants, solvents, apparel, adhesives and similar supplies. See Section 130.330(c)(3). However, pneumatic hand tools or electric powered hand tools used primarily in manufacturing or assembling may qualify for the exemption.

In addition to the exemption for manufacturing machinery and equipment, the State of Illinois provides a manufacturer's purchase credit (MPC) on the purchase of tangible personal property that qualifies for the manufacturing machinery and equipment exemption. See the enclosed copy of 86 Ill. Adm. Code 130.331. Manufacturers who have earned MPC on the purchase of qualifying manufacturing machinery and equipment can use that accumulated MPC to satisfy their Use Tax or Service Use Tax liability on the purchase of production related tangible personal property. Please note that the amount of MPC that can be applied to a purchase of production related tangible personal property is limited to the state rate of tax incurred on that property (6.25%). Any local taxes incurred on the purchase of production related tangible personal property remain the responsibility of the purchaser.

POLLUTION CONTROL DEVICES

For your general information, we have enclosed a copy of 86 Ill. Adm. Code 130.335, which governs the pollution control facilities exemption. No items qualify for the Pollution Control Facilities exemption in and of themselves. In order to qualify for the pollution control facilities exemption, a facility must be a "system, method, construction, device or appliance appurtenant thereto sold or used or intended for the primary purpose of eliminating, preventing, or reducing air and water pollution, ... or for the primary purpose of treating, pretreating, modifying or disposing of any potential solid, liquid or gaseous pollutant which if released without such treatment, pretreatment, modification or disposal might be harmful, detrimental or offensive to human, plant or animal life, or to property." If the primary purpose of the equipment is to serve an economic purpose, it will not qualify for the exemption.

Paint booths or some of the component parts of paint booths may qualify for the exemption. Due to the limited amount of information in your letter describing the paint booths, we are unable to provide you with more specific information.

SALES OF SERVICE

Illinois Retailers' Occupation and Use Taxes do not apply to sales of service that do not involve the transfer of tangible personal property to customers. However, if tangible personal property is transferred incident to sales of service, this will result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon which tax base the servicemen choose to calculate their tax liability. For your general information we are enclosing a copy of 86 Ill. Adm. Code 140.101 regarding sales of service and Service Occupation Tax.

Under the Service Occupation Tax Act, businesses providing services (i.e. servicemen) are taxed on tangible personal property transferred as an incident to sales of service. See the enclosed copy of 86 Ill. Adm. Code 140.101. The purchase of tangible personal property that is transferred to the service customer may result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon which tax base the servicemen choose to calculate their tax liability. The servicemen may calculate their tax base in one of four ways: (1) separately stated selling price of tangible personal property transferred incident to service; (2) 50% of the servicemen's entire bill; (3) Service Occupation Tax on the servicemen's cost price if the servicemen are registered de minimis

servicemen; or (4) Use Tax on the servicemen's cost price if the servicemen are de minimis and are not otherwise required to be registered under the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale of service. The tax is then calculated on the separately stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred as an incident of the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers.

Your letter indicates that your client does not separately state the selling price of the paint or other tangible personal property transferred incident to its sales of service. Therefore, it cannot utilize the first method listed above. If your client utilizes the second or third tax bases listed above, the materials which will be incorporated into manufactured goods and resold may be purchased free of tax as sales for resale. This can include such items as paint as long as the paint is incorporated into the items for resale. The requirements for a valid Certificate of Resale are set out in the enclosed copy of 86 Ill. Adm. Code 130.1405(b). Likewise, purchases of packaging materials may be purchased for resale as long as they are transferred along with the products contained in them to customers. See in the enclosed copy of 86 Ill. Adm. Code 130.2070(a). Such purchasers must provide their suppliers with Certificates of Resale to document the exemption. Please note, however, that containers would not qualify for the exemption if, after delivery, the seller of the tangible personal property contained in them retained and reused them or discarded them.

If your client qualifies for and utilizes the last tax base described above, it cannot purchase any items for resale. It must pay tax to its suppliers or remit Use Tax directly to the Department as described above.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b) described above.

Very truly yours,

Terry D. Charlton
Associate Counsel

TDC:msk
Enc.